Santa Barbara Airport

Structuring Considerations

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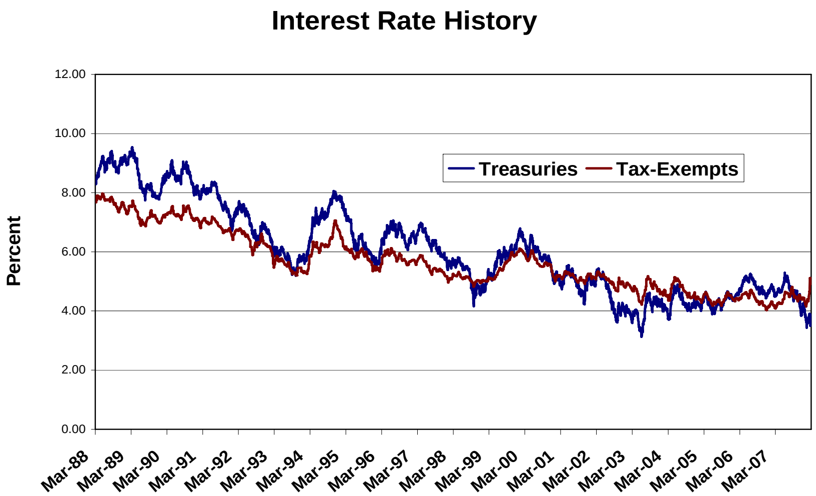
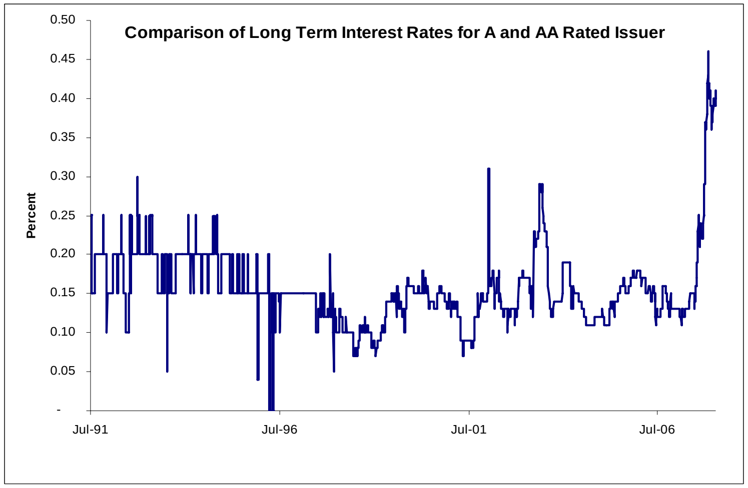
Update on the Municipal Bond Market

Update on the Municipal Market

- Sub-prime mortgage crisis and impact on collateralized debt obligation market have created volatile market conditions and have led to a global contraction in liquidity.
- Long-term interest rates are relatively low but extremely volatile
  - Changes in municipal market index of 50 basis points (one-half percent) over the course of only one week..
- Credit spreads (the difference in yield between AAA and lower rated credits) have widened rapidly due to a general flight to quality
  - Appetite for "plain vanilla".
- Municipal yields exceed treasury yields.
  - Loss of hedge funds as buyers, who are now flooding the secondary market
  - Expectations of significant new issuance as variable rate is converted to fixed rate
  - Limited capacity of traditional institution investors.





Market Roiled by Crisis of Bond Insurers

- Only 2 bond insurers carry "AAA" market value.
- Increased insurance premiums and less availability.

Insurance Ratings Update as of March 7, 2008

Lesser Concern

Greater Concern

	Moody's		S&P [1]		Fitch	
	Rating	Outlook	Rating	Outlook	Rating	Outlook
FSA	Aaa	Stable outlook 12/14/07	AAA	Stable outlook 12/19/07	AAA	Stable outlook 1/25/08
Assured	Aaa	Stable outlook 12/14/07	AAA	Stable outlook 12/19/07	AAA	Stable outlook 11/22/07
MBIA	Aaa	Negative outlook 2/26/08	AAA	Negative outlook 2/25/08	**AAA**	**Negative credit watch, 2/5/08**
Ambac	**Aaa**	**Negative credit watch 1/17/08**	**AAA**	**Negative credit watch 2/25/08**	**AA**	**Negative credit watch 1/18/08**
CIFG	**A1**	**Stable outlook 3/6/08**	AAA	Negative outlook 2/28/08	**AA-**	**Negative credit watch 3/7/08**
FGIC	**A3**	**Negative credit watch 2/14/08**	**A**	**Negative credit watch 2/25/08**	**AA**	**Negative credit watch 1/30/08**
Radian	Aa3	Stable outlook 12/14/07	AA	Stable outlook 12/19/07	**A+**	**Negative outlook 9/5/07**
XL	**A3**	**Negative outlook 2/7/08**	**A-**	**Negative credit watch, 2/25/08**	**A**	**Negative credit watch 1/23/08**
ACA	N/A	N/A	**CCC**	**Negative outlook 12/19/07**	N/A	N/A

Credit Strategy for Airport Terminal Expansion Financing

Project Overview

- Two major projects will require debt financing
  - Terminal renovation and expansion project
  - Rental car facility

- Debt will be secured three sources of funds
  - Passenger Facility Charges (PFCs)
  - Customer Facility Charges on car rentals (CFCs)
  - General airport revenues

Uses of Funds	
New Terminal	$33,230,000
Historical Building	$2,340,000
Roadways	$1,420,000
Parking	$5,170,000
Airside	$8,500,000
New Carrier Space	$1,560,000
Total Anticipated Terminal Cost	$52,220,000
Rental Car Facility	$6,450,000
Construction Contingency	$3,720,000
Soft Cost	$10,190,000
Total Uses of Funds	$72,580,000

Sources of Funds	
Federal	$16,550,000
Department Funds	$4,268,000
Passenger Facilities Charges	$4,944,000
Customer Facility Charges	$1,360,000
Bonds proceeds	$43,000,000
Funding Shortfall	$2,458,000
Total Sources of Funds	$72,580,000

Summary Structuring Considerations

- A key financing question is whether to secure bonds only with general airport revenues (GARB), or to back the revenue bonds with a contingent pledge of the City's General Fund
- Revenue bonds would be secured exclusively by a pledge of net airport revenues (gross revenue minus operating expenses), including PFC and CFC
  - Market requires that net revenues be at least 1.5 times debt service
- A "double barrel" structure would provide for paying debt with airport revenues, but backing that pledge bonds with General Fund
  - Would eliminate the requirement for coverage from the bond market
  - City may want some cushion to protect General Fund
    - Projected airport revenues provide approximately 1.20 times debt service coverage at current rates
- Use of General Fund backing is expected to be necessary to finance the project as currently envisioned
- City's General Fund has capacity to support such a financing
  - Virtually no current General Fund debt ($3 million in Certificates of Participation)
  - Airport bonds would be viewed as substantially "self-supporting" by rating agencies
    - Therefore, not likely to affect General Fund's ability to impact debt

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Analysis of Structuring Considerations

- The City's underwriter, Morgan Stanley, ran analysis based on the following assumptions:
  - AMT bond issue based on current market conditions
  - Bond amount includes taxable rental car facility issue and inclusion of CFC revenues
  - Other assumptions based on Jacobs Consultancy presentation
- Estimated total debt service savings of $1.2 million with a secondary revenue pledge from the City
  - Present value of debt service savings equal to approximately $572,000
- Using current market rates to calculate debt service on a standalone GARB issue and CFC-backed rental car facility issue results in combined debt service coverage of 1.37x in FY2013.

Standalone Airport Revenue Bonds

- Expected Ratings:
  - Baa1/BBB+
- Target Coverage Level:
  - 1.5x coverage
- Expected Insurance Premium:
  - 100 basis points, *if available*
- Debt Service Reserve Fund:
  - Funded at Maximum Annual Debt Service

Standalone Airport Revenue Bonds Debt Statistics	
Par Amount:	$42,125,000
Total Debt Service:	$86,275,800
Net Debt Service	$81,819,825
Average Annual DS:	$2,875,860
Maximum Annual DS:	$2,924,900
All-In TIC:	5.60%

Airport Revenue Bonds with City Pledge

- Expected Ratings:
  - A1/A+
- Target Coverage Level:
  - 1.0x coverage
- Expected Insurance Premium:
  - 40 basis points
- Debt Service Reserve Fund:
  - Funded at Maximum Annual Debt Service

Airport Revenue Bonds with City Pledge Debt Statistics	
Par Amount:	$41,535,000
Total Debt Service:	$85,057,375
Net Debt Service:	$80,663,850
Average Annual DS:	$2,835,245
Maximum Annual DS:	$2,883,762
All-In TIC:	5.49%

Sensitivity Analyses

Project Fund Deposit

- Morgan Stanley calculated estimated surplus or shortfall for a combined $36.5 million terminal financing and a $6.5 million taxable rental car financing.
  - As shown, a standalone GARB financing produces an approximately $5.7 million funding shortfall at $7.50 per enplaned passenger using a 1.5x coverage target.
  - A City-backed issue provides a surplus of approximately $14.5 million at $7.50 using a 1.0x coverage target.
    - Sufficient to cover up to a 33.7% project cost increase.

Sensitivity Analysis: City-Backed Issue
Project Fund Deposit Based on 1.0x Coverage Target

	Terminal Project Only		
Airline Payment Per Enplanement	Project Cost	Proceeds Generated	Surplus/ (Shortfall)
$7.50	$43,000,000	$57,492,872	$14,492,872
$5.00	$43,000,000	$40,578,104	($2,421,896)

Sensitivity Analysis: City-Backed Issue (Rates + 100 bps)
Project Fund Deposit Based on 1.0x Coverage Target

	Terminal Project Only		
Airline Payment Per Enplanement	Project Cost	Proceeds Generated	Surplus/ (Shortfall)
$7.50	$43,000,000	$49,101,969	$6,101,969
$5.00	$43,000,000	$34,724,180	($8,275,820)

Sensitivity Analysis: Standalone GARB Issue
Project Fund Deposit Based on 1.5x Coverage Target

	Terminal Project Only		
Airline Payment Per Enplanement	Project Cost	Proceeds Generated	Surplus/ (Shortfall)
$7.50	$43,000,000	$37,337,501	($5,662,499)
$5.00	$43,000,000	$26,249,699	($16,750,301)

Sensitivity Analysis: Standalone GARB Issue (Rates + 100 bps)
Project Fund Deposit Based on 1.5x Coverage Target

	Terminal Project Only		
Airline Payment Per Enplanement	Project Cost	Proceeds Generated	Surplus/ (Shortfall)
$7.50	$43,000,000	$31,751,343	($11,248,657)
$5.00	$43,000,000	$22,370,506	($20,629,494)

Preliminary Conclusions

- Project would not be affordable assuming customary market assumptions.
  - Assuming a Standalone GARB financing, based on the Feasibility Consultant's projections, as well as estimated debt service costs, it does not appear that the whole project is affordable at a 1.5x debt service coverage target.
- Current market will make it even more difficult and expensive to issue bonds backed exclusively with an airport revenue pledge.
- A City-backed financing would accommodate entire project as currently budgeted and still provide cushion to General Fund.
- Planning on a City-pledge would benefit the Airport by providing a financial safety net in case the airline rates and charges are set below the targeted $7.50, the cost of the project increases, or the bond market further deteriorates.

Additional Information

Comparable Airport Data: A3 Rated O&D Airports with less than 1 MM Enplanements

- Santa Barbara's forecasted cost per enplanement of $7.50 is within the range of A3 rated airports' 2006 results.
- Recommended debt service coverage target of at least 1.50x would be consistent with A3 rated airports.
- Santa Barbara Metropolitan Statistical Area (MSA) population approximately 400,335.

Selected Financials and other Datapoints	Bishop International Airport, MI	Columbia Metropolitan Airport, SC	Jackson-Evers International Airport, MS	Lansing Capital City Airport, MI	Pensacola Regional Airport, FL	Portland International Jetport Airport, ME
General Entity Information						
Fiscal Year End	12/31/2006	12/31/2006	9/30/2006	6/30/2006	9/30/2006	6/30/2006
Senior Most Rating (Moodys/S&P/Fitch)	A3/A-/NR	A3/NR/NR	A3/NR/A-	A3/NR/NR	A3/BBB+/BBB+	A3/BBB+/NR
Airport Type	O&D	O&D	O&D	O&D	O&D	O&D
Rate Making Methodology	Ordinance	Residual	Hybrid	Compensatory	Residual	Compensatory
Primary Carrier	Northwest	Delta	Southwest	Northwest	Delta	US Airways
Enplanements ('000)	536	642	753	304	811	680
Enplanement five year CAGR (%)	12.0	3.9	2.2	0.1	9.1	0.1
O&D enplanements (%)	100	100	98	100	100	99
Primary carrier market share (%)	40	35.4	33.4	52.1	44	30.2
Top two carriers market share (%)	76.7	54.8	62	69.5	60	55
Service area population ('000)	444	697	541	456	447	516
Utilization ratio	1.21	0.92	1.36	0.67	1.82	1.3
Net funded debt ($ '000)	28,305	79,129	40,792	11,255	31,794	42,724
Income Statement Data and Ratios						
Operating revenues ($ '000)	12,458	16,147	14,674	7,351	14,669	11,814
Airline payments ($ '000)	965	4,013	4,539	3,233	4,641	4,559
Gross revenue and income ($ '000)	13,108	21,020	14,896	10,790	15,391	12,260
Net income ($ '000)	5,029	9,702	4,471	2,602	5,962	2,372
GARB debt service ($ '000)	2,633	6,481	1,934	1,440	2,851	2,254
Operating ratio (%)	64.8	70.1	71	111.4	64.3	83.7
Airline payments per enplanement ($)	1.8	6.25	6.03	10.65	5.72	6.7
Airline payments/operating revenues (%)	7.7	24.9	30.9	44	31.6	38.6
Days Cash on Hand	511	207	330	270	152	356
Debt and Debt Service Ratios						
Debt ratio (%)	17.2	49.3	30.1	18.6	33.6	35.7
Debt per enplaned passenger ($)	56.83	139.51	64.34	41.19	42.43	66.32
Debt service coverage by net income (x)	1.91	1.50	2.31	1.81	2.09	1.05
Debt service coverage per bond ordinance (x)	2.79	1.66	3.08	2.73	1.84	1.40

Source: Moody's Municipal Financial Ratio Analysis and Morgan Stanley

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Additional Information

Comparable Airport Data: Baa1 Rated Airports O&D Airports with less than 1 MM Enplanements

Selected Financials and other Datapoints	Burlington International Airport, VT	Corpus Christi International Airport, TX	Eugene Airport, OR	Fresno Yosemite International Airport, CA	Rogue Valley International - Medford Airport, OR
General Entity Information					
Fiscal Year End	6/30/2006	7/31/2006	6/30/2006	6/30/2006	6/30/2006
Senior Most Rating	Baa1/NR/BBB+	Baa1/BBB-/BBB	Baa1/NR/NR	Baa1/BBB/BBB+	Baa1/NR/NR
Airport Type	O&D	O&D	O&D	O&D	O&D
Rate Making Methodology	Hybrid	Hybrid	Hybrid	Hybrid	Hybrid
Primary Carrier	US Airways	Southwest	United Express	United Express	Horizon
Enplanements ('000)	692	445	357	619	300
Enplanement five year CAGR (%)	5.9	0.9	-1.4	4.3	5.0
O&D enplanements (%)	100	100	100	100	100
Primary carrier market share (%)	24.5	36	45.5	33.1	39.8
Top two carriers market share (%)	47.9	68.9	74.2	54	77.9
Service area population ('000)	206	417	339	1,020	195
Utilization ratio	3.36	1.07	1.05	0.61	1.54
Net funded debt ($ '000)	47,271	19,986	1,594	35,412	19,355
Income Statement Data and Ratios					
Operating revenues ($ '000)	10,216	8,132	8,107	14,669	5,235
Airline payments ($ '000)	2,984	2,662	2,341	3,690	1,939
Gross revenue and income ($ '000)	12,275	8,401	8,291	18,043	6,595
Net income ($ '000)	5,007	1,209	2,750	4,474	2,702
GARB debt service ($ '000)	3,824	1,585	620	2,961	0
Operating ratio (%)	71.1	88.4	68.3	92.5	74.4
Airline payments per enplanement ($)	4.31	5.98	6.56	5.96	6.46
Airline payments/operating revenues (%)	29.2	32.7	28.9	25.2	37
Days Cash on Hand	242	376	520	96	157
Debt and Debt Service Ratios					
Debt ratio (%)	47.6	21.4	2.1	26.8	NA
Debt per enplaned passenger ($)	69.57	46.16	5.48	65.24	NA
Debt service coverage by net income (x)	1.31	0.76	4.44	1.51	NA
Debt service coverage per bond ordinance (x)	1.31	1.34	4.74	7.42	NA

Source: Moody's Municipal Financial Ratio Analysis.

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